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Lovestruck Royalty snares its prey at last

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Royalty Pharma must today feel as elated as a lover whose target finally succumbs after years of giving the brush-off. And not only has it snared Tysabri, the object of its longstanding attention, it has picked it up for a fraction of what it had earlier been willing to pay.

Nevertheless, Tysabri expectations have been falling, and an analysis of sellside consensus forecasts suggests that even at the lower price Royalty risks overpaying (see table below). Still, Royalty looks nowhere near as foolish as Perrigo, which it is now clear had vastly overpaid for Tysabri back in 2013.

Not that the Tysabri interest, which came along with Elan, was the reason for Perrigo's $8.6bn purchase of the Irish company. Back in 2013, when Royalty was narrowly defeated in the bidding, what Perrigo was after was Elan's low-tax Irish domicile.

By domiciling in Ireland Perrigo reckoned to save some $150m per year after tax – an asset that Berenberg analysts said was worth around $1.5bn (*Perrigo uses strong shares to engineer a handy tax deal, July 29, 2013*).

Deducting that and the $1.9bn of Elan's cash on hand meant that Perrigo thought the Tysabri interest – Elan's only other asset – was worth around $5bn. Clearly, given the $2.9bn maximum value of yesterday's deal with Royalty, this now looks to have been a mistake; Perrigo stock was off 12% this morning, though this probably also had to do with the resignation of its chief financial officer.

Market erosion

While the risks of Tysabri have become better understood its market is being eroded by oral multiple sclerosis drugs, and its future is clouded by novel entrants like Roche's Ocrevus. Two years ago sellside consensus put 2020 Tysabri sales at over $2.5bn, but this now stands at just $1.6bn, *EvaluatePharma* computes.

As such even $2.9bn might see Royalty overpaying. What Royalty has bought is simply an 18% royalty of Biogen's global sales – the royalty rises to 25% on annual sales above $2bn, which now looks unattainable – which even using a generous 7.5% cost of capital equates to a pretax NPV of just $1.7bn.

Tysabri royalty: what Royalty is buying for $2.9bn...							
	2017	**2019**	**2021**	**2023**	**2025**	**2027**	**2029**
Biogen Tysabri sales ($m)	1,915	1,664	1,527	1,450	1,386	1,331	1,285
Perrigo's 18% royalty ($m)	345	300	275	261	249	240	231
WACC	7.5%						
NPV ($m)	***1,717***						
...versus what Perrigo paid in 2013							
Net Perrigo paid for Elan in 2013 ($m)	6,700						
Value of Elan tax asset ($m)	1,500						
Value of Tysabri royalty 2013-16 ($m)	900						
Implied net value assigned to Tysabri royalty in 2013 ($m)	***4,300***						
Source: EvaluatePharma sellside consensus forecasts.							

Of course, Royalty's purchase might indicate that the sellside is being too bearish. Tysabri's key patents are thought to expire in 2024, but of course the entry of biosimilars, especially in the US, can still only be guessed at.

Long term

Shortly after buying Elan Perrigo admitted that it had no intention of becoming a branded pharma company, fuelling more speculation that it would divest the Tysabri interest.

But it was not to be, and only last November, with its stock off 40% over the previous 12 months, did the company implement a “review of strategic alternatives”. As *EP Vantage* had speculated back in 2013, Royalty was always the most logical buyer.

Subtracting the nearly $1bn of royalties that Perrigo will have received for 2013-16 sales still leaves the group over $4bn short of the asset’s value at the time of the Elan deal. This shortfall now looks embarrassing for Perrigo, but when you are in a dead-end relationship it makes sense to cut and run.

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